



Service Credit Payment Options

for school employees purchasing service credit

Purchasing service credit, whether with pre- or post-tax money, can have a long-range financial impact. The Office of Retirement Services (ORS) encourages you to review this information with a financial planner and/or tax consultant before deciding whether to purchase service credit and which method of payment would be best for you. For more information on different service credit types and purchasing service credit, request a copy of the *Enhancing Your Pension* booklet, or explore the school employees' website at www.michigan.gov/ors, for more information.

Purchasing by Direct Payment

If you wish to make a direct payment for any or all of the service credit reflected on your *Member Billing Statement*, do the following:

- (1) Prepare a check or money order payable to **State of Michigan–ORS**. Include your name and social security number on the remittance.
- (2) Send your payment with a copy of your *Member Billing Statement* to:

Office of Retirement Services
Finance Division
P.O. Box 30673
Lansing, MI 48909-8173

If you prefer to make your payment in person, please note that we can only accept payments at our main office in Lansing. Our representatives in Detroit cannot accept any payment. For directions, visit our website.

Purchasing by Tax-Deferred Payment

You can request that payments for your service credit purchase be deducted from your wages. This payment method, called tax-deferred payments, or TDP, gives you an easy payment plan plus a significant tax break. The amount you authorize for deduction from your biweekly paycheck is not subject to income tax until you begin receiving your pension at retirement.

While the tax advantages are great, you should be aware that a TDP agreement, once initiated, is *binding and irrevocable*. This means that once you have completed the enrollment process with your payroll officer and deductions have begun, deductions cannot stop until the agreement is complete, or you terminate employment. The IRS also mandates that you cannot have constructive receipt of the tax-deferred funds you use to purchase service credit. Once you establish a TDP agreement to purchase a set amount of service credit, payments must be made through payroll deduction only. You cannot have possession of the funds and then pass them to the retirement system; funds must pass directly from the employer to the retirement system.

Once you **begin** payments with a **TDP** agreement, you **cannot** stop or lower your deductions.

Your employer must have passed a resolution allowing participation in the TDP program. Check with your payroll office to see if you can use TDP to buy service credit.

Interest on TDP Balances.

When you and your payroll officer sign a TDP agreement, your cost for the purchase is locked. It will not increase as your age, rate of pay, or years of service increases. However, once a TDP agreement has been in effect for a full year, any balance you carry past June 30 will be assessed interest, currently 8 percent.



www.michigan.gov/ors



P.O. Box 30171, Lansing, MI 48909-7671



(800) 381-5111

Note: The interest provision on TDP balances became effective January 1, 2004. Any TDP agreement established before then will not be assessed interest.

Your annual *Member Statement* will detail your payments in the past year, show interest applied, and your agreement pay off balance.

For example, if your TDP agreement began on July 15, 2004, interest would be added to your remaining balance July 1, 2006. In the table below, lines 3, 4, and 5 illustrate how 8 percent interest is applied annually to your unpaid TDP agreement balance.

	Year 1	Year 2	Year 3	Year 4
1. Total due at the beginning of the year	\$30,000	→\$22,000	→\$12,960	→\$ 3,197
2. Amount paid	8,000	10,000	10,000	3,197
3. Balance before interest	22,000	12,000	2,960	-
4. 8% Interest (line 3 x .08)		960	237	-
5. TDP agreement balance (line 3 = line 4)	22,000	12,960	3,197	-
6. Total years of service credit purchased to date	1.33	3.000	4.5432	5.0 years

Using the table above, you will notice that line 6 shows how much credit has been purchased at the end of each year. So, if you leave public school employment at the end of year 3, you will be credited with 4.5432 years of service.

Note: If you are vested, pro-rata credit will be granted for universal buy-in, military, maternity/paternity/child rearing leave, post-1974 out-of-system public education service, non public education service, and sabbatical leave service before leaving employment. All other billing types must be paid in full, before service will be credited.

Deciding how much to have withheld.

The maximum allowable TDP deduction is your gross compensation, less any required deductions such as social security and Medicare, or other levies or garnishments. Your payroll office can help you determine your maximum deduction.

The minimum withholding per TDP agreement is \$50 a pay period. If you're not sure how much you want held out of your paycheck, remember that even if your financial circumstances change later, you can't decrease or stop your deduction. You can, however, increase your deduction on an ongoing basis whenever you wish.

You can also have multiple TDP deductions simultaneously. You may want to set up an agreement to purchase some of the service credit on your current billing statement, and then when you can afford it, initiate an additional agreement. To do so, you simply request an updated billing statement and then establish a new TDP agreement with your payroll office. Remember, though, that each new agreement has its own \$50 minimum deduction, and will be based on the cost in effect at the time the agreement is signed and approved.

There is no minimum or maximum time limit. Your TDP agreement can be for as few or as many pay periods as you wish. We encourage you to plan to have your purchase completed well in advance of retirement. It's also smart to reduce your balance as quickly as possible because of the interest that's added each year.

TDPs and deferred compensation deductions.

TDP deductions do not count *as* 403(b) deductions nor do they count *against* 403(b) deductions. Since TDP deductions are taken before 403(b) deductions, however, they lower the amount of your compensation available to be contributed to 403(b) plans.

How to sign up for the TDP program.

If you decide to purchase any or all of the service credit shown on your *Member Billing Statement* through the TDP program, complete the *TDP Agreement* form that accompanies your billing statement. Your payroll office can help you complete the form.

Return the agreement to your payroll office with a copy of your *Member Billing Statement* (be sure to keep a copy for your records). The payroll officer will review, sign and date the form, and take action to begin your payroll deductions. Watch your pay statements. If your deductions don't begin in a reasonable period of time, be sure to follow up with your payroll office. It is your responsibility to make sure that the deductions have started and are correct.

Note: If you intend to purchase out-of-system or nonpublic education service from different employers, you can ask ORS to combine billing statements of a similar type before you initiate a TDP agreement. That way, you'll have one scheduled deduction with one deduction per pay period rather than multiple TDP agreements, each with a \$50 minimum deduction per pay period.

An important note about due dates.

The date your payroll officer signs the form is the effective date of the agreement. That date must be earlier than the "due date" shown on your *Member Billing Statement*, or the agreement is invalid. If the due date has passed before your enrollment is completed, you must obtain an updated *Member Billing Statement* from ORS and complete a new TDP agreement form.

Increasing your scheduled deductions.

Your TDP agreement is established for a fixed deduction amount per pay period. While this deduction cannot be stopped or reduced, you can increase the amount of your payroll deduction. For information on how to increase your deduction, contact your payroll officer or download the *Supplemental TDP Agreement* from our website.

What to do if your employment changes.

Your TDP agreement remains valid while you are on unpaid leave or temporarily off payroll for any reason, as long as an employer-employee relationship exists. Your payroll office should resume your deductions when you return to work.

If you change your employer to another Michigan public school, you can sign a new agreement to continue the payments. The new agreement must be signed within 90 days after you have terminated with your previous employer to retain the service credit cost from your prior agreement. It is your responsibility to provide your new payroll office with a copy of your previous agreement.

If 90 days have passed, you'll have to set up a new TDP agreement. Ask ORS for a recalculated *Member Billing Statement* and complete a new agreement form as described earlier in this section.

If you leave public school employment with a TDP balance.

If you leave school employment before you're able to pay off your TDP balance, you have a few options for the remainder. How you handle it depends on whether you need the credit to qualify for retirement benefits.

- **Get partial credit.** Prorated credit will be granted for TDP agreements not paid in full for universal buy-in, military, maternity/paternity/child rearing, nonpublic education, and post-1974 out-of-system public education employment purchases.

Prorated credit will not be granted for TDP agreements not paid in full for pre-July 1981 sabbatical leave, pre-1974 out-of-system public education service, state of Michigan service, or weekly workers' compensation. To receive credit for these service credit types, your balance must be paid in full.

- **Increase your scheduled deductions.** You can increase your deductions each pay period, or request that all or part of any final compensation, such as accrued leave payoffs, be applied toward your purchase. For either option, contact your payroll office. Remember that required deductions such as social security and Medicare taxes are withheld from any final compensation first, so have your payroll office help you figure the net amount you have available.

Your **billing statement** must be **current** to purchase service credit. Most statements **expire** at the end of the **fiscal year**.

- **Direct payment or plan-to-plan transfer.** You can make a direct payment, or you can “roll over” funds from a qualified retirement plan such as your 401(k) or 403(b) plan to pay off your TDP balance (see Purchasing with a Qualified Plan-to-Plan Transfers). To apply a qualified plan transfer or direct payment against your TDP balance, you must either: (1) have filed a retirement application, or (2) have a bona fide termination of your employment within 90 days after ORS receives payment. It is also important to coordinate your payoff with ORS because your TDP balance changes with each pay date. An ORS customer service representative can help you determine your balance, explain the procedure to follow, and provide the necessary forms.

Purchasing with a Qualified Plan-to-Plan Transfer

A **qualified plan-to-plan transfer** is the process of moving money from a qualified (as defined by IRS) pretax investment account/retirement plan to another without incurring taxes or penalties on the money being transferred.

The IRS recently expanded these definitions, so now you can “roll over” money you have saved in most pretax retirement accounts and use it to purchase service credit. A qualified plan can be your 401(a), 401(k), 403(b), 457, as well as conduit IRAs (Individual Retirement Accounts) from any of these sources. A traditional IRA cannot be used to purchase service credit.

How to request a plan-to-plan transfer.

If you decide to purchase any or all of the service credit shown on your *Member Billing Statement* by transferring from a qualified plan, request or download a *Qualified Plan-to-Plan Transfer Certification* form from our website.

This form includes detailed instructions on how to initiate a plan-to-plan transfer. Complete and return it to ORS so that we know the dollar amount you intend to transfer to purchase service credit. It is then your responsibility to arrange with your plan administrator to send the payment directly to ORS.

Be sure to allow ample time for your plan administrator to transfer the funds. Some financial institutions take several weeks, or even months. This can result in an additional cost to you if the payment arrives after the due date. It is important for your payment to arrive before the due date or your retirement date—remember, we cannot accept any payment for service credit after you have terminated public school employment.

Be sure to **allow**
4 - 6 weeks
to complete your
plan-to-plan transfer.

When ORS receives your qualified plan-to-plan transfer payment, you'll be issued a receipt and your retirement account will be updated with your service credit purchase.

Plan-to-plan transfers are handled between ORS and the investment institution holding your funds (your plan administrator) acting on your request. Your payroll office should not be involved.

Plan-to-plan transfers must be for the exact amount of the purchase.

Be sure that your plan administrator doesn't send more than the amount shown on your *Member Billing Statement*, because taxes and penalties could apply. If too much money is submitted, the excess funds will be returned to the institution holding the qualified plan, if possible. Otherwise, the excess may be refunded to you, and taxes and penalties may apply.

Purchasing with a Transfer and TDP

You can combine methods of payment to purchase service credit. However, if you plan to purchase some service credit using a plan-to-plan transfer and some through tax-deferred payroll deductions, complete the transfer *before* you enter into a TDP agreement.

If you are terminating or retiring before your TDP agreement is paid in full, you may be able to apply a plan-to-plan transfer to the TDP balance. If these conditions apply to you, contact ORS for assistance. We will help you determine the balance and complete the proper forms.

